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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Amendment of the Part 69 Allocation	)	CC Docket No. 92-222
of General Support Facility Costs	)	

COMMENTS OF MFS COMMUNICATIONS COMPANY, INC.

MFS Communications Company, Inc. ("MFS"), by its undersigned counsel, submits these comments in response to the Notice of Proposed Rulemaking that was contained in the Commission's *Special Access Expanded Interconnection Order* (the *"Order"*).[1]

In this docket, the Commission is considering amending 47 CFR § 69.307 to modify the method for allocating the General Support Facilities ("GSF") category of net investment among the various interstate access service elements, which in turn would affect the access charges imposed by local exchange carriers ("LECs"). General Support Facilities is defined in 47 CFR § 69.2(q) as follows:

> "General Support Facilities" include buildings, land, vehicles, aircraft, work equipment, furniture, office equipment and general purpose computers as described in the *Separations Manual* and included in Account 2110.

The current rule requires allocation of this category of investment based on the allocation (under other rules) of investment in central office equipment, information origination/

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[1] *Expanded Interconnection with Local Telephone Company Facilities*, CC Dockets No. 91-141 and 92-222, Report and Order and Notice of Proposed Rulemaking, FCC 92-440 (released October 19, 1992). The Notice of Proposed Rulemaking appears at paragraphs 267-69 of the *Order*.

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termination equipment, and cable and wire facilities ("C&WF") excluding Category 1.3. Since Category 1.3 contains investment in subscriber loop plant, this exclusion results in a reduction in the amount that would otherwise be allocated to the Common Line category. *See Order*, paras. 147, 267. The Commission has proposed to remove the exclusion of Category 1.3 C&WF investment, which would result in a substantial increase in the investment allocated to the Common Line element, and offsetting reductions in the allocations to all other access elements. *Id.* This amendment would also have similar effects on the allocations of various expense categories that are based upon the GSF investment allocation. *Id.*, nn.624-25. The combined effect of these several categories on the LECs' overall expense allocations would, MFS believes, be quite substantial.

The GSF category contains a wide range of assets, including such items as corporate airplanes, office buildings, computers, and even the proverbial "president's desk," which are not readily attributable to the provision of any single communications service. These assets are "common costs" in the economic sense, since they are used in producing all of a telephone company's services and probably do not vary with the level of output of any particular service element. In addition, the category contains some assets (such as computers, motor vehicles, and office furniture that are used by employees whose work pertains only to a single access element) that *are* attributable in principle to particular services.[2]

The Commission has proposed to amend the allocation rule because it believes that the current allocation creates a "non-cost-based support flow" to Common Line from other access elements, including especially Special Access and Transport. *Order*, para. 147. By implication, the Commission evidently believes that an allocation based on the proportion of each access element's allocated investment in other classes of assets would be more "cost-based" than the current rule. As a matter of economic theory, however, there is *no* "correct" cost-based method of allocating common costs. Any such allocation method is *inherently* arbitrary.[3] The Commission's proposal would merely replace one arbitrary method of allocating common costs with a different arbitrary method. And, to the extent that the GSF category includes non-common costs, the only economically correct method of allocation would be one that examined actual cost causation. Although the use of an arbitrary allocation may potentially be justified on grounds of practicality,[4] the Commission should not lose sight of the fact that it *is* arbitrary.

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[2] For example, a desk, chair, and desktop computer used by an employee whose sole responsibility is the evaluation and procurement of Class 5 central office switches would be attributable in theory to the local switching element exclusively; but the Commission's existing and proposed rules would allocate these investments among all of the access elements.

[3] *See* Baumol, Koehn & Willig, *How Arbitrary is "Arbitrary"?—or, Toward the Deserved Demise of Full Cost Allocation*, 120 PUB. UTIL. FORTNIGHTLY 16 (Sept. 3, 1987).

[4] It is conceivable that the costs of the additional recordkeeping and analysis necessary to allocate GSF investments to particular services would exceed the benefits of a more precise allocation.

Given that any allocation rule is necessarily arbitrary, the Commission must determine whether the proposed rule would serve the public interest better than the existing one does. MFS respectfully suggests that, in making this judgment, the Commission should bear in mind the underlying purposes of its cost allocation rules, which include the prevention of unjust and unreasonable pricing by dominant carriers. While the Commission must, of course, permit the LECs a reasonable opportunity to recover their overhead costs from their customers, its rules should not assign an excessive portion of these costs to any class of customers or any service category, unless there is a clearly-defined public interest reason for doing so. As the LECs face the beginnings of significant competition in some of their service markets, they will have a natural incentive to seek to reduce the amount of overhead and other costs recovered from the more competitive service elements, and to increase the amount recovered from those elements that are still effectively monopoly services. Absent regulatory constraints, the LECs would tend to increase the prices of their monopoly rate elements to the point where the revenue derived from any further price increase would be offset by a reduction in demand. This point is the profit-maximizing price which, in economic theory, is characteristic of unregulated monopoly pricing. One of the fundamental purposes of economic regulation of the communications industry, of course, is specifically to prevent regulated entities from engaging in monopoly pricing.

The Commission's objective should be to require each service element to bear a portion of the common costs that approximates the amount that could be recovered in a competitive market. If an element is assigned more than this competitive portion of the costs, then either ratepayers will be forced to pay monopoly rates for that service (if it is in fact a monopoly, as are most LEC services), or else the LEC will be unable to recover the assigned costs (if the market is effectively competitive). Conversely, if a competitive rate element is assigned an unduly low share of common costs, the LEC's service will have an unjustified market advantage. The actual and prospective competitors of the LECs also have overhead and common costs,[5] and they also must set their rates at levels that enable them to recover these costs on a company-wide basis; it would therefore be anti-competitive to permit the LECs to offer competitive services without having to recover *any* common overhead costs from the rates charged for those services.

In this case, the Commission has not proposed to eliminate the allocation of GSF investment and other common costs to special access and switched transport services, but has merely proposed to reduce the proportion allocated to these categories. This change may be justified if the Commission determines that its proposed allocation will more closely reflect the hypothetical operation of market forces in a fully competitive market than does the present rule. If not, the Commission should consider adopting a different allocation procedure for these costs.

In the event that the Commission adopts the proposed rule, it should also address how the LECs should reflect their changed costs in the design of special access rates.

[5] For example, MFS makes investments and incurs costs that are comparable to some of the GSF category investments, such as office space rentals, furniture, general purpose computers and other office and work equipment. MFS does not, however, own or operate any aircraft.

For price cap LECs, the price cap rules provide only limited guidance, as discussed below, while for rate of return LECs there are no specific rules dictating the design of rates below the special access category level. *See* 47 CFR § 69.114. Because the Commission has proposed this allocation change in order to eliminate "non-cost-based support flows," it should require that the resulting rate changes be directed to those specific special access elements that currently are providing the support flows.

Significantly, the Commission considered this very issue in determining to change its cost allocation rules rather than adopt a "contribution charge" to allow recovery of the full GSF allocation within the special access category. The Commission found that:

> it is very difficult to determine how much of the GSF support flows are included in rates for LEC services subject to competition—*i.e.*, DS1 and DS3 services. Most of the Tier 1 price cap LECs have substantially reduced their DS1 and DS3 rates in recent years, and it therefore appears likely that rates for such services recover *significantly less* GSF support amounts than do other special access services.

Order, para. 148 (emphasis added). In light of these findings, it is essential that the Commission prescribe safeguards to assure that "significantly less" of the rate reduction resulting from GSF reallocation be taken from DS1 and DS3 rates than from other special access services.[6]

[6] The Price Cap rules do not dictate such a result. To the contrary, when NYNEX recently proposed an interim reallocation of its GSF expenses using the Price Cap rules, it offered a *larger* percentage reduction for DS1 services than for any other category of special access services, despite the fact that the DS1 price cap subindex was already quite close to the lower limit of its pricing flexibility band even before this proposed adjustment. *See* NYNEX Tariff FCC No. 1, Transmittal No. 137 (filed Nov. 18, 1992; proposed effective date Jan. 2, 1993).

Conclusion

MFS respectfully urges that any rules adopted in this proceeding be consistent with the principles set forth in the foregoing comments.

Respectfully submitted,

Andrew D. Lipman RMB

Andrew D. Lipman
Russell M. Blau
SWIDLER & BERLIN, Chartered
3000 K Street, N.W.
Washington, D.C. 20007
(202) 944-4300

Attorneys for MFS Communications Company, Inc.

Of Counsel:

Cindy Z. Schonhaut
Vice President-Government Affairs
MFS Communications Company, Inc.
3000 K Street, N.W., Suite 300
Washington, D.C. 20007
(202) 944-4209

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CERTIFICATE OF SERVICE

I hereby certify that on this 4th day of December, copies of Comments of MFS Communications Company, Inc., were served by hand delivery on the following:

Alfred C. Sikes
Chairman
Federal Communications Commission
1919 M Street, N.W.
Suite 814
Washington, D.C. 20554

James H. Quello
Commissioner
Federal Communications Commission
1919 M Street, N.W.
Suite 802
Washington, D.C. 20554

Andrew Barrett
Commissioner
Federal Communications Commission
1919 M Street, N.W.
Suite 844
Washington, D.C. 20554

Douglas Slotten, Esq.
Policy & Program Planning Division
Federal Communications Commission
1919 M Street, N.W.
Suite 544
Washington, D.C. 20554

James Schlichting
Chief, Policy & Program Planning Division
Federal Communications Commission
1919 M Street, N.W.
Suite 544
Washington, D.C. 20554

Ervin S. Duggan
Commissioner
Federal Communications Commission
1919 M Street, N.W.
Suite 832
Washington, D.C. 20554

Sherrie P. Marshall
Commissioner
Federal Communications Commission
1919 M Street, N.W.
Suite 826
Washington, D.C. 20554

Cheryl Tritt
Common Carrier Bureau
Federal Communications Commission
1919 M Street, N.W.
Suite 500
Washington, D.C. 20554

Downtown Copy Center
Federal Communications Commission
1990 M Street, N.W.
Room 640
Washington, D.C. 20036

Celia Petrowsky

Celia Petrówsky